

**Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, DC 20554**

**In the Matter of**

**Verizon Telephone Companies  
Petition for Forbearance from  
the Current Pricing Rules for  
the Unbundled Network Element  
Platform**

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**Docket No. WC 03-157**

**COMMENTS OF THE NEW JERSEY  
DIVISION OF THE RATEPAYER ADVOCATE**

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August 18, 2003

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**COMMENTS OF THE NEW JERSEY  
DIVISION OF THE RATEPAYER ADVOCATE**

The New Jersey Division of the Ratepayer Advocate ( New Jersey Ratepayer Advocate ) herewith submits its comments in response to the Verizon Telephone Companies Petition for Forbearance from the Commission s Current Pricing Rules for the Unbundled Network Element Platform ( Petition ).<sup>1</sup> In the Petition, Verizon Telephone Companies ( Verizon or the Company ) ask the Commission to forbear from (1) applying its current total element long-run incremental cost ( TELRIC ) pricing rules to the unbundled network element platform ( UNE-P ), and (2) permitting UNE-P carriers to collect per minute access charges from long distance carriers. As discussed in more detail below, the New Jersey Ratepayer Advocate respectfully submits that Verizon s Petition should be denied or, in the alternative, dismissed.

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<sup>1/</sup> The Federal Communications Commission ( Commission ) issued a Public Notice on July 3, 2003, (DA 03-2180) in WC Docket No. 03-157, which set the comment and reply comment period for this matter. Subsequently, on July 15, 2003, the Commission released an Order granting an extension of time to file comments until August 18, 2003, and to file reply comments until September 2, 2003. See *I/M/O Verizon Telephone Companies Petition for Forbearance From the Current Pricing Rules for the Unbundled Network Element Platform*, Order (DA 03-2333) (rel. Jul. 15, 2003).

## I. INTRODUCTION.

Verizon's Petition ignores the fact that the Company's challenges to the UNE-P were fully litigated before and subsequently rejected by the Commission<sup>2</sup> and the United States Supreme Court.<sup>3</sup> Verizon is improperly using Section 10 of the Telecommunications Act of 1996<sup>4</sup> to avoid the *res judicata* effects of its failed litigation strategy. It would be inconsistent with the public interest to permit Verizon to achieve through a forbearance petition what it could not accomplish through litigation. The Petition represents nothing more than the Company's attempt at a second bite of the apple. The New Jersey Ratepayer Advocate respectfully requests the Commission to reject the Company's latest effort to frustrate and impede the opening of telecommunications markets to full and healthy competition.

Verizon's request for the Commission to abandon its position on UNE-P is contrary to the Commission's announced position in the Triennial Review, wherein the Commission found that UNE-P was presumptively necessary to bring the benefits of competitive alternatives to all

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<sup>2/</sup> See, generally, *I/M/O Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Interconnection Between Local Exchange and Commercial Mobile Radio Service Providers: First Report and Order*, CC Docket Nos. 96-98, 95-185, 11 FCC Rcd 15,449 (rel. Aug. 8, 1996) ( *First Report and Order* ). Appendix A of the First Report and Order lists the commenters in this proceeding, which include Bell Atlantic Telephone Companies and GTE Service Corporation, corporate predecessors to Verizon.

<sup>3/</sup> *Verizon Communications, Inc. v. Federal Communications Commission*, 122 S.Ct. 1646 (2002) ( *Verizon v. FCC* ) .

<sup>4/</sup> Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 ( 1996 Act ). The 1996 Act amended the Communications Act of 1934. Hereinafter, the Communications Act of 1934, as amended by the 1996 Act, will be referred to as the Act, and all citations to the Act will be to the Act as it is codified in the United States Code.

consumers.<sup>5</sup> In order to forbear from applying its regulations, the Commission must find that continuation of the UNE-P and modification of its access charge policies (1) are not necessary to ensure just, reasonable, and nondiscriminatory services, (2) are not necessary for the protection of consumers, and (3) that elimination is otherwise consistent with the public interest.<sup>6</sup> In applying these criteria, the Commission must consider whether forbearance would promote competition among telecommunications service providers.

## **II. THE CURRENT PRICING RULES THAT APPLY TO UNE-P ARE SENSIBLE AND HAVE WITHSTOOD SUPREME COURT REVIEW.**

The New Jersey Ratepayer Advocate opposes the Verizon petition to eliminate UNE-P. Abandonment of UNE-P would preclude residential competition and frustrate the goals of the Act. Verizon has failed to offer any evidence (let alone compelling evidence) that would support its claims that the conditions for granting forbearance have been met.<sup>7</sup> Similarly, Verizon has not demonstrated that grant of this Petition would promote competitive market conditions and otherwise promote competition among providers of telecommunications services. In fact, grant of the Petition would wreak a severe and adverse effect on competition and conditions within the competitive markets, and otherwise reverse, frustrate, and eliminate established pro-competitive Commission policies initiated in 1996 and subsequently reaffirmed in the Commission's

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<sup>5/</sup> See FCC Adopts New Rules for Local Network Unbundling Obligations of Incumbent Local Phone Carriers, Federal Communications Commission News Release (Feb. 20, 2003).

<sup>6/</sup> See 47 U.S.C. § 160.

<sup>7/</sup> See 47 U.S.C. § 151 et seq, and Section 10 of the Act, codified at 47 U.S.C. § 160.

Triennial Review Order.<sup>8</sup> There is no evidence in this record that demonstrates that the public interest would be served by grant of the Petition.

Verizon claims that the Commission's UNE pricing rules discourage investment, impede competition, and undermine economic growth.<sup>9</sup> Verizon asserts that TELRIC pricing for UNEs is flawed because it is based upon a hypothetical network that results in below cost rates which do permit Verizon to recover its investment. Verizon also claims that the pricing methodology provides too much latitude to States in setting rates without regard to costs, as evidenced by UNE rate reductions by various state commission proceedings since TELRIC adoption in 1996.<sup>10</sup> Verizon, however, fails to account for the fact that prices are adjusted as state commissions gain expertise, and as cost models are developed and refined. The Company ignores the fact that telecommunications is a declining cost industry, and that the public switched telephone network was paid for by ratepayers. The Company also ignores the fact that states have paid due care to BOC interests. As noted by the Phoenix Center for Advanced Legal and Economic Policy Studies ( Phoenix Center ), the States have actually preserved some BOC profit in a politically-sensible 50/50' split between the desired outcomes of new entrants and the incumbents.<sup>11</sup> Further, Verizon's claims that it has been forced as part of Section 271 proceedings to drop its

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<sup>8/</sup> See FCC Adopts New Rules for Local Network Unbundling Obligations of Incumbent Local Phone Carriers, Federal Communications Commission News Release (Feb. 20, 2003).

<sup>9/</sup> See *Petition for Forbearance of the Verizon Telephone Companies* ( *Petition* ), at 1.

<sup>10/</sup> *Id.* at 2, 3

<sup>11/</sup> T. Randolph Beard and George S. Ford, *What Determines Wholesale Prices for Network Elements in Telephony? An Economic Education*, Phoenix Center Policy Paper No. 16 (Sep. 2002) (available at <http://www.phoenix-center.org/pcpp/PCPP16.pdf>).

rates in order to obtain in-region long distance approval<sup>12</sup> is wholly without merit. If that is the case, then Verizon should have disputed the TELRIC UNE rates at that time, rather than to wait until after it has benefitted from its implementation of what it now calls a flawed process.<sup>13</sup>

Verizon touts reports prepared by independent analysts that allege that regulators are forcing BOCs like Verizon to provide UNE-P at below-cost rates.<sup>14</sup> In doing so, the Petitioner seeks to disregard a mechanism that has been upheld by the Supreme Court. The Petitioner has failed to submit data that discredits the appropriateness of the current Commission approach to fostering competition in the local exchange marketplace. Indeed, the elimination of UNE-P would have the effect of stifling competition in its infancy.

The instant analysis benefits from a comparison to the Commission's dominant/non-dominant analyses, because the ability to discriminate against other carriers is of the same magnitude in both instances. The Commission's dominant/non-dominant inquiries are intended to preserve the same type of pro-competitive and non-discriminatory atmosphere as envisioned by Section 10 of the Act. The Ratepayer Advocate submits that before forbearance can be granted, the Commission must determine that sufficient competition to constrain the incumbents

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<sup>12</sup>/ *Petition* at 2, 3.

<sup>13</sup>/ Specifically, Verizon concludes:

This rapid reduction in UNE-P rates is not the result of some corresponding reduction in the costs of providing UNEs. Instead, this steady downward trend has been driven by pressure to produce the appearance of competition by providing CLECs what they claim is a sufficient profit margin between UNE prices and retail prices, which themselves are often artificially low to , make it worth their while to compete in a given state. *Id.* at 3.

<sup>14</sup>/ *Id.* at 3, 4.

market power exists in current markets. The New Jersey Ratepayer Advocate submits that Verizon must show that it is non-dominant in order to support its Petition. The Company has offered no evidence to show that it is non-dominant. Accordingly, the Commission must reject the Petition.

This renewed attack on TELRIC follows the Company's failed litigation strategy over the past six years to challenge TELRIC and the rates derived from its use. Verizon is regurgitating prior arguments already rejected twice by the Supreme Court. In *Verizon Communications, Inc. v. FCC*, 122 S.Ct. 1646 (2002) (note 3, *supra*), the Supreme Court flatly rejected Verizon's attack on the legality and logic of the TELRIC pricing methodology. Verizon's basic criticism of TELRIC is that by setting rates for leased network elements on the assumption of perfect competition, TELRIC creates perverse incentives against competition. Specifically, Verizon complains that TELRIC sets rates so low that entrants will always lease and never build network elements, and that instead of promoting competition, CLECs will engage in free-riding that will take the place of facility-based competition.<sup>15</sup> Verizon, however, conveniently ignores the fact that the Supreme Court validated TELRIC as a proper method of setting rates under the Act:

We cannot say whether the passage of time will show competition prompted by TELRIC to be an illusion, but TELRIC appears to be a reasonable policy for now, and that is all that counts. The incumbents have failed to show that TELRIC is unreasonable on its own terms, largely because they fall into the trap of mischaracterizing the FCC departures from the assumption of a perfectly competitive market (the wire-center limitation, regulatory and development lags, or the refusal to prescribe high depreciation and capital costs) as inconsistencies rather than pragmatic features

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<sup>15</sup>/ *Petition* at 8, 9.

of the TELRIC plan. Nor have they shown it was unreasonable for the FCC to pick TELRIC over alternative methods, or presented evidence to rebut the entrants figures as to the level of competitive investment in local-exchange markets. In short, the incumbents have failed to carry their burden of showing unreasonableness to defeat the deference due the Commission. We therefore, reverse the Eight Circuit s judgment insofar as it invalidates TELRIC as a method for setting rates under the Act.<sup>16</sup>

Further, in direct contradiction to the claims set forth by Verizon in the instant Petition, the Supreme Court flatly rejected the claim that TELRIC limits facilities-based investment:

At the end of the day, theory aside, the claim that TELRIC is unreasonable as a matter of law because it simulates but does not produce facilities-based competition founders on the fact. The entrants have presented figures showing that they have invested in new facilities to the tune of \$55 billion since the passage of the Act . . . The FCC s statistics indicate substantial resort to pure and partial facilities-based competition among the three entry strategies . . . The incumbents do not contradict these figures, but merely speculate that the investment has not been as much as it could have been under other ratemaking approaches, and they note that investment has more recently shifted to nonfacilities entry options.<sup>17</sup>

The Supreme Court reversed the Eighth Circuit decision to set aside the Commission s combination rules when it held:

In sum, what we have are rules that say an incumbent shall, for payment, perform the functions necessary, to combine network elements to put a competing carrier on an equal footing with the incumbent when the requesting carrier is unable to combine when it would not place other competing carriers at a competitive disadvantage. This duty is consistent with the Act s goals of

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<sup>16</sup>/ *Verizon v. FCC* at 1678, 1679 (internal citations omitted).

<sup>17</sup>/ *Id.* at 1675.

competition and nondiscrimination, and imposing it is a sensible way to reach the result the statute requires.<sup>18</sup>

The Supreme Court has upheld the validity of TELRIC and its application to UNE-P. Verizon's attempt to secure forbearance of those rules after it has failed in its judicial attempts amounts to nothing more than an effort to skirt *res judicata* and accomplish administratively what it was unable to achieve judicially. A letter from AT&T to the Commissioners in the Triennial Review proceeding noted the irony of such a position:

[t]he provisions of the 1996 Act are so clear that the incumbent LECs *agreed* with AT&T and other CLECs [on the issue of states involvement] . . . during the first six years of proceedings to implement the local competition provisions of the 1996 Act. The incumbents have now cynically changed their position because they understand that State commissions have detailed knowledge of competition that the incumbents are urging the Commission to reject.<sup>19</sup>

Here, too, the Petitioner is doing an about-face as it urges total elimination of UNE-P. For the reasons set forth above and below, the Commission should reject the Company's Petition.

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<sup>18</sup>/ *Id.* at 1687 (internal citations omitted).

<sup>19</sup>/ Letter from Marc C. Rosenblum, Vice-President, Law, AT&T to Michael K. Powell, Chairman, Kathleen Q. Abernathy, Commissioner, Jonathan S. Adelstein, Commissioner, Michael J. Copps, Commissioner, and Kevin J. Martin, Commissioner, Federal Communications Commission, at 4 (Dec. 18, 2002) (emphasis in original).

**II. THE CURRENT PRICING RULES ARE ECONOMICALLY VALID, PROMOTE COMPETITION, AND WILL GENERATE BENEFITS FOR CONSUMERS AND THE INDUSTRY.**

**A. The Company's Claims that UNE-P has Devalued and Discouraged Investment are Unsupported and Contradicted by Industry Experts and Basic Economic Theory.**

Verizon argues unpersuasively that the UNE-P pricing rules have devalued the telecommunications infrastructure. Verizon's sole support for this theory of devalued investment is the market capitalization drop in the industry since 2000.<sup>20</sup> According to Verizon, market capitalization of the telecommunications and equipment manufacturing sectors has declined by some \$2 trillion.<sup>21</sup> Verizon's assumption that UNE pricing is responsible for this substantial drop is simplistic and fails to account for other possible causes. In the first instance, the telecom and Internet bubble that prompted unrestrained spending for new facilities and capacity affected telecom investment. This frenzy collided with failed business plans of competitive local exchange carriers. Unfortunately, Verizon offers no evidence as to the effect of overbuilding and the collapse of the telecom and Internet sectors on investment. The Company ignores these events and the resultant shock waves that echoed throughout the industry, and instead blames reduced telecom investment on Commission rules that are actually constructed in such a manner so as to promote competition. As explained further herein, UNE-P enables rational network build-out that is based on active and growing market share, rather than the widespread broad speculation that preceded the tech stock/telecom meltdown of 2000. Verizon's claims that the

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<sup>20</sup>/ *Petition* at 5.

<sup>21</sup>/ *Petition* at 5.

pricing rules allow carriers with no facilities to drain billions of dollars in revenue away from facilities-based competitors<sup>22</sup> is without merit.

Verizon asserts that the drop in investment by wireline telecommunications carriers from \$104.8 billion to \$42.8 billion between 2000 and 2002 coincides with the decline in UNE rates.<sup>23</sup> Incredibly, Verizon attributes all of the decline to the pricing of the UNEs, without any accounting for other influences, including the downturn in the economy and the recessionary cycle. Indeed, empirical evidence indicates that BOCs actually invest *more* in UNE-P states. As noted by the Phoenix Center, [w]hile poor economic conditions are curtailing investment in most sectors of the economy, including telecommunications, the specific effect of UNE-P on investment is positive. <sup>24</sup>

Verizon ignores even the general notion that infrastructure investment over time cannot continue unabated. Peaks followed by reduced investment are part of the normal economic cycles. Under Verizon's assumption, the stock market would have continued to rise indefinitely. The Company's repeated refrain that below-cost UNE rates affect infrastructure investment adversely is a claim unsupported by the facts. As made clear by the Phoenix Center, [t]o date, there is no reliable econometric evidence of which we are aware that indicates unbundling discourages investment by either BOCs or CLECs, or otherwise has any negative impact on

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<sup>22</sup>/ *Petition* at 6.

<sup>23</sup>/ *Petition* at 7.

<sup>24</sup>/ *Competition and Bell Company Investment in Telecommunications Plant: The Effects of UNE-P*, Phoenix Center Policy Bulletin No. 5, at 4 (Jul. 9, 2003) (available at <http://www.phoenix-center.org/PolicyBulletin5.pdf>).

economic performance in the telecommunications industry.<sup>25</sup> Verizon has made no showing that the current regulatory environment, including rate cap regulations, is not adequately compensating Verizon. Indeed, the Company's supposed concern for disincentives to invest and resultant impact on its profits are not reflected in the compensation that it pays to top executives. As reflected in publically filed documents, Verizon's Chief Executive Officer ( CEO ) received stock options valued at \$58.4 million in 2002, and the CEO and other executives received over \$427 million over the last six years.<sup>26</sup> Ultimately, if Verizon actually believed that its financial performance was in jeopardy, Verizon could just request a return to rate of return regulation. Then, Verizon would be assured a reasonable return on its infrastructure investments. To date, Verizon has not sought such relief.

**B. Verizon Fails to Offer Appropriate Granular Data, and Relies Instead Upon an Inappropriate Mix of National and State Data.**

Verizon relies upon anecdotal evidence to suggest that net profits available from use of the UNE-P create a disincentive for CLECs to invest in facilities because CLECs can allegedly generate more money by using the UNE-P.<sup>27</sup> However, there is no support for how these so called profit margins are calculated, or whether such margins are available ubiquitously throughout a state, let alone all states. Verizon extrapolates its conclusions from a generalized statement and then attempts to use those theories to buttress its calls for the elimination of the

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<sup>25</sup>/ *Id.* at 5.

<sup>26</sup>/ *See* Tom Johnson, Verizon Answers Union Ads with Campaign of Its Own, Newark Star Ledger (Jul. 23, 2003); *see, also*, CWA Members Vote Verizon Strike Authorization if Contract Talks Falter, Communications Workers of America Press Release (Jul. 17, 2003).

<sup>27</sup>/ *Petition* at 8.

UNE-P on a national scale. The New Jersey Ratepayer Advocate submits that reliance upon very generalized observations, and application of them on a national basis without a state-by-state analysis is inadequate support for the Company's positions. Even more striking is that Verizon fails to offer appropriately granular data in this regard. Instead, the Company uses state-specific UNE rate reductions in limited markets to support its plea for national elimination of UNE-P. Further, the Company does not supply a state-by-state empirical analysis.

No clearer example of this superficial analysis is Verizon's claim that CLECs have curtailed the use of their existing facilities in favor of the UNE-P. Verizon asserts that CLECs in eight states connected more than 600,000 fewer lines to their own switches in 2002 than they did in 2000.<sup>28</sup> Then, Verizon points to the fact that competing carriers on a national basis added more than nine million UNE-P lines.<sup>29</sup> Verizon's observation, however, proves nothing because it is an apples to oranges comparison. The decline in the eight states may be attributable to the financial deterioration of CLECs, as evidenced by the number of bankruptcies filed in the telecommunications arena. The nine million lines increase on a national level lacks any detail or support as to the correlation between UNE-P rates in a particular state and the increased ordering of the UNE-P. There is no evidence as to whether the increased usage of the UNE-P is occurring in those states where the UNE rates have been lowered. Verizon's arguments lack any probative value as to the assertions made.

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<sup>28</sup>/ *Petition* at 9.

<sup>29</sup>/ *Id.*

The Commission has recognized the necessity of granular analysis, stating the relevant geographic market for regulatory investigation should be defined, narrowly enough so that competitive conditions within each area are reasonably similar, yet broadly enough to be administratively workable.<sup>30</sup> Commissioner Kevin J. Martin, too, emphasized the importance of granular analysis in matters related to local competition. Citing a United States Court of Appeals decision, Commissioner Martin noted that the Commission took into account specific geographic market conditions in the triennial review, recognizing that competitors face different operational and economic barriers in different markets.<sup>31</sup> Grant of the Petition would cut the states, and their specialized local expertise, out of the TELRIC process. The states, however, have necessary local experience, as demonstrated by UNE-P costs that vary from state to state, reflecting the individual characteristics of geographic areas and incumbent telephone companies. As stated by the American Conservative Union in a letter to the Commission in the Triennial Review proceeding,

state PUCs are closer to the specific needs of consumers the states are suited to implement the competitive promise and Congressional intent of the Telecommunications Act that consumers should have a choice of local telephone companies.<sup>32</sup>

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<sup>30/</sup> *I/M/O Access Charge Reform; Price Cap Performance for Review for Local Exchange Carriers; Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers; Petition of US West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA: Fifth Report and Order and Further Notice of Proposed Rulemaking*, CC Docket Nos. 92-262, 941, CCB/CPD File No. 98-63, CC Docket No. 98-157, 14 FCC Rcd 14,221, at para. 71 (Aug. 27, 1999) ( *Pricing Flexibility Order* ) .

<sup>31/</sup> Commisisoner Kevin J. Martin s Press Statement on the Triennial Review, Feb. 20, 2002, at 2.

<sup>32/</sup> Letter from American Conservative Union to Federal Communications Commission (Dec. 11, 2002).

The Company failed to provide data for all states and inappropriately imputed limited state-specific data to an attempted nationwide application. The Company failed to make the necessary *prima facie* showing, and its Petition should therefore be dismissed.

### **III. THE PETITIONER FAILS TO MEET ANY OF THE STANDARDS FOR FORBEARANCE.**

#### **A. The Current Pricing Rules are Necessary to Ensure that Charges, Practices, Classifications, or Regulations are Just and Reasonable and are Not Unjustly or Unreasonably Discriminatory.**

Section 10 of the Act sets forth three prongs of the forbearance test, of all which must be met before a petition for forbearance can be approved. The standards are: (1) enforcement . . . is not necessary to ensure that the charges, practices, classifications, or regulations . . . are just and reasonable and are not unjustly or unreasonably discriminatory; (2) enforcement . . . is not necessary for the protection of consumers; and (3) forbearance . . . is in the public interest.<sup>33</sup> As stated by the DC Circuit in *Cellular Telecommunications and Internet Association, et al. v. Federal Communications Commission, et al.*,<sup>34</sup> [t]he three prongs . . . are conjunctive . . . [t]he Commission could properly deny a petition for forbearance if it finds that any of the three prongs is unsatisfied.<sup>35</sup> The New Jersey Ratepayer Advocate will demonstrate herein that Verizon has failed to satisfy any of the prongs.

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<sup>33</sup>/ 47 U.S.C. § 160.

<sup>34</sup>/ *Cellular Telecommunications and Internet Association, et al. v. Federal Communications Commission, et al.*, U.S. Court of Appeals, No. 02-1264 (slip op.) ( *CTIA* ) (2003).

<sup>35</sup>/ *CTIA* at 12.

The *CTIA* court ruled that the necessary standard of the second prong does not mean absolutely required or indispensable.<sup>36</sup> Instead, the court explained that while the term can mean required to achieve the desired goal, it need not be the only approach toward meeting that goal.<sup>37</sup> The *CTIA* court cited judicial review of Section 251(c)(6) in *GTE Service Corp. v. FCC*, 205 F.3d 416, 423 (D.C. Cir. 2000), wherein the court stated that necessary does not foreclose a particular means to an end merely because other means are hypothetically available. . .<sup>38</sup>

The Company argues that the entire mechanism of TELRIC should be eliminated. This startling conclusion, however, must be examined in light of the Commission's commitment to the UNE-P, and states' and industry's reliance on it as a pathway toward competition. Indeed, UNE-P enables competition because it gives consumers a choice of telecommunications providers. Further, even customers who remain with the incumbent local exchange carrier ( ILEC ) benefit from the competition, because the competitive pressures force the ILEC to meet CLEC offerings. Commissioner Martin noted this phenomenon when he noted, It is true that there are now a significant number of residential telephone customers that receive service from a CLEC, but *the overwhelming majority of these customers is currently served through an incumbent's switch.*<sup>39</sup>

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<sup>36</sup>/ *CTIA* at 13.

<sup>37</sup>/ *CTIA* at 14.

<sup>38</sup>/ *CTIA* at 14.

<sup>39</sup>/ Commisisoner Kevin J. Martin's Press Statement on the Triennial Review, Feb. 20, 2002, at 2 (emphasis added).

When the Company's Petition is examined in the context of other forbearance petitions, notably, those that have addressed issues of dominance and non-dominance, Verizon's Petition must be rejected. The Commission stated that in the *Pricing Flexibility Order*, it adopted a framework that would grant price-cap LECs greater flexibility as greater competition developed for high-capacity special access and dedicated transport for switched access services ( high capacity services ). The Commission, however, stated that the flexibility must not enable LECs to deter efficient entry or engage in exclusionary pricing behavior, or increase rates to unreasonable levels where consumers lacked competitive alternatives.<sup>40</sup>

In review of BOC petitions for forbearance, the Commission first examined the first prong of the forbearance test and stated that the BOCs were required to make a *prima facie* showing that the application of relevant Commission regulations was no longer necessary to ensure that the rates and practices for the services in question were just, reasonable, and non-unreasonably discriminatory.<sup>41</sup> The New Jersey Ratepayer Advocate submits that this test requires that *all* elements be satisfied i.e., that the rates are just, and that the practices are just; that the rates are reasonable, and that the practices are reasonable, etc. The Commission found

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<sup>40</sup>/ I/M/O Petition of US West Communications, Inc., for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA; Petition of the SBC Companies for Forbearance from Regulation as a Dominant Carrier for High Capacity Dedicated Transport Services in Specified MSAs; Petition of US West Communications, Inc., for Forbearance from Regulation as a Dominant Carrier in the Seattle, Washington MSA; Petition of Bell Atlantic Telephone Companies for Forbearance from Regulation as Dominant Carriers in Delaware, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, Washington, D.C., Vermont, and Virginia; Petition of Ameritech for Forbearance from Dominant Carrier Regulation of its Provision of High Capacity Services in the Chicago LATA: Memorandum Opinion and Order, CC Docket Nos. 98-157, 98-227, 99-1, 99-24, 99-65, FCC 99-365 (rel. Nov. 22, 1999), at para. 12 ( *US West, et al.* ), citing *Pricing Flexibility Order*.

<sup>41</sup>/ *Id.* at para. 32.

that the BOCs failed to meet this burden, in part, because the data relied upon by the BOCs was flawed and unsubstantiated. In this regard, the Commission looked only at market share, without addressing (1) the supply elasticity of the market, (2) the demand elasticity of the petitioner's customers, and (3) the petitioner's cost structure, size, and resources. The Commission also found that certain of the market definitions utilized in the market reports that were relied upon by the BOCs did not portray accurately the true state of affairs. This, in turn, resulted in distort[ed] data on the BOCs stated position on competitive inroads made by other carriers.<sup>42</sup> The same infirmity exists in the instant Petition, which, as described before, draws allegedly national conclusions from limited data that arises out of only eight states. Accordingly, the instant Petition is similarly defective and should be rejected.

The Petitioner premises its position in part on the assertion that incumbent LECs are losing market share to competitors who have no incentive to construct facilities. As discussed in *AT&T Corp. v. FCC*, 236 F.3d 729 (DC Cir. 2001), the Commission was criticized for addressing only one of multiple factions. The court noted that the Commission itself acknowledged that [t]he Commission traditionally considered in classifying carriers as dominant or non-dominant include market share, supply substitutability, elasticity of demand, and the cost structure, size, and resources of the carrier.<sup>43</sup> The court seems to suggest that the Commission's non-dominant analysis is relevant in any forbearance review, unless the Commission explains why another or different analysis is appropriate. The New Jersey Ratepayer Advocate submits

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<sup>42</sup>/ *Id.* at para. 33.

<sup>43</sup>/ *AT&T Corp. v. FCC* at 736.

that a non-dominant analysis is appropriate in all Section 10 proceedings that seek to remove regulatory control from market dominant entities. Verizon offers no such analysis and the Company has failed to make a *prima facie* case. Therefore, the Company's Petition should be dismissed.

Upon appeal, the court remanded the *US West, et al.*, decision back to the Commission because, according to the court, the Commission departed from its traditional non-dominance analysis without explanation.<sup>44</sup> The court noted that in prior determinations that Commission had relied upon more factors than just the market share analysis. In the *U.S. West, et al.*, decision, however, the Commission had considered only market share. As noted by the Court, [i]n the past, the FCC has considered market share along with other factors such as supply elasticity, demand elasticity and comparative advantages in cost structure, size and resources<sup>45</sup> Verizon's instant Petition sets forth data that alleges to support the proposition that continued use of UNE-P will discourage facilities-based competition as envisioned by the Act. The Petition, however, lacks any discussion on whether Verizon is no longer dominant in the local exchange market, and fails to provide or otherwise address supply and demand elasticities and other structure, size, and resource comparisons with alleged competitors.

**B. The Current Pricing Rules are Necessary to Protect Consumers.**

The Petitioner has ignored conveniently the preamble of the Act, which states that it is intended to promote competition and reduce regulation in order to secure lower prices and

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<sup>44</sup>/ See *AT&T Corp. v. FCC*.

<sup>45</sup>/ *AT&T Corp. v. FCC* at 731. Indeed, *US West* contemplated these factors in its filing, *see id.* at 732.

higher quality services *for American telecommunications consumers* and encourage the rapid deployment of new telecommunications technologies.<sup>46</sup> The focus of the Act is toward consumers, and choices available to them. Nowhere has it been shown that continued use of UNE-P is inconsistent with the Act. Experience has shown that resale and use of the incumbent's facilities is a necessary step toward establishing sufficient market entry that would justify subsequent facilities-based investment in a network. The Petitioner cannot have it both ways if Verizon bemoans the state of the telecommunications industry's financial health, then it cannot momentarily later argue that competitive carriers should be coerced into establishing expensive redundant networks. For example, in the long distance market, both MCI and Sprint resold and utilized the AT&T network when first entering the market in the 1970s. It was only after market share was established that the carriers moved from less-expensive self-owned microwave transitions toward more comprehensive and expensive fiber loops.<sup>47</sup> The time spent utilizing slender pieces of self-owned equipment alongside the facilities of AT&T enabled the competitive carriers to capture market share that would justify the more expensive network investments. In the instant proceeding, use of the UNE-P, *even without any self-owned facilities*, is a critical step toward the creation of competitive networks.

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<sup>46</sup>/ Act, pmb1., 110 Stat. 56. *See also Goldwasser v. Ameritech Corp.*, 222 F.3d 390, at 391 ("bring the benefits of deregulation and competition to all aspects of the telecommunications market in the United States, including especially local markets").

<sup>47</sup>/ *See* Huber, Kellogg, and Thorne, *Federal Telecommunications Law* at § 9.3.2, Aspen Law and Business (1999), citing *citing* D. L. Kaserman & J. W. Mayo, Long Distance Telecommunications Policy Rationality on Hold, Pub. Util. Fort., Dec. 22, 1988, at 21-22.

The Act provides for three methods of competition: CLEC-built facilities, resale of ILEC services, and the use of UNEs, including UNE-P. The Supreme Court recognized this imperative, stating:

When it promulgated its unbundling rules, the Commission explicitly declined to impose a requirement of facilities ownership on carriers who sought to lease network elements . . . the effect of this omission was so to allow competitors to provide local phone service relying solely on the elements in an incumbent's network.<sup>48</sup>

The Supreme Court did not leave any doubt when it upheld the validity of the unbundling structure, stating,

we think that the Commission reasonably omitted a facilities-ownership requirement. The 1996 Act imposes no such limitation; if anything, *it suggests the opposite*, by requiring in § 251(c)(3) that incumbents provide access to any requesting carrier.<sup>49</sup>

The Petitioner fails to show how UNE-loop service is insufficient to promote the goals of the Act. Whereas with UNE-P a competitor can serve virtually any customer, anywhere, UNE-loop requires collocation in the incumbent's central office, a proposition that is sensible only if the CLEC has a significant number of customers in that wire center that justifies the cost. UNE-P, by contrast, enables a CLEC to slowly build market share across a wide area before transitioning to UNE-loop, and ultimately to full-facilities-based (whether those facilities be a redundant local loop or other technology). An ILEC may maintain several thousand central office buildings; it would be improbable that a start-up CLEC would have sufficient customers in

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<sup>48</sup>/ *AT&T Corp. v. Iowa Utilities Board*, 119 S. Ct. 721, 728, 729 (1999) (internal citations omitted).

<sup>49</sup>/ *Id.* at 736 (emphasis added).

each wire center to justify the cost of collocation in each central office. As the Commission recognized in the *Pricing Flexibility Order*,

collocation usually represents a financial investment by a competitor to establish facilities within a wire center. . . . [T]he investment in transmission facilities associated with collocation arrangements is largely specific to a location; the competitive LEC's facilities cannot, for the most part, be easily removed and used elsewhere if entry does not succeed.<sup>50</sup>

The New Jersey Ratepayer Advocate recognizes that competition need not be from another wireline infrastructure. Indeed, the Act states plainly the goal of encourag[ing] the rapid deployment of new telecommunications technologies. In the words of Justice Breyer,

The Act expresses this last-mentioned sharing requirement in general terms, reflecting congressional uncertainty about the extent to which compelled use of an incumbent's facilities will prove necessary to avoid waste. Will wireless technology or cable television lines, for example, permit the efficient provision of local telephone service without the use of existing telephone lines that now run home to home?

Despite the empirical uncertainties, the basic congressional objective is reasonably clear. The unbundling requirement seeks to facilitate the introduction of competition where practical, *i.e.*, without inordinate waste.<sup>51</sup>

Wireless communications may well provide burgeoning competition to traditional wireline, as may cable and IP-based communications. The New Jersey Ratepayer Advocate submits that UNE-P based competition, complementing other technologies, permits the broadest exploration of competitive options, and is most in keeping with the Act's goal of promoting competition.

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<sup>50</sup>/ *Pricing Flexibility Order* at 81.

<sup>51</sup>/ *Id.*, *Separate Opinion of Justice Breyer, Concurring in Part and Dissenting in Part*, at 753.

Verizon, like the other BOCs, enjoys a network that was constructed and paid for by captive ratepayers during a period of regulated monopoly protection. In the instant matter, the Petitioner relies primarily upon anecdotal accounts from newspapers and other articles, but fails to provide the hard data on why elimination of UNE-P promotes the Act's goals of competition. The Petitioner has failed to make a *prima facie* showing that it is non-dominant and that Section 10 forbearance is warranted.

**C. Forbearance from the Pricing Rules Would be Inconsistent with and Contrary to the Public Interest.**

The Petitioner alludes to the practice of cherry picking, or cream skimming, whereby a competitive carrier will take a low-cost approach (such as UNE-P) to secure the business of only several but highly profitable customers (i.e., high-volume business lines).<sup>52</sup> This concern is not new to the telecommunications industry, which confronted similar issues at the advent of long-distance competition.<sup>53</sup> The conclusion of the saga, which included much opposition to new entrants such as MCI and Sprint, is telling:

MCI and Sprint have since abandoned their microwave beginnings for fiber optics. Yet microwave transmission technology was crucial to the development of competition in the long-distance marketplace. It reduced overall entry costs for new firms, while simultaneously allowing carriers to enter with geographically mobile fixed assets rather than the traditional telephone cables that were literally sunk costs.<sup>54</sup>

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<sup>52</sup>/ Petition at 10.

<sup>53</sup>/ See Huber, Kellogg, and Thorne, *Federal Telecommunications Law* at § 9.3.2, Aspen Law and Business (1999).

<sup>54</sup>/ *Id. citing* D. L. Kaserman & J. W. Mayo, Long Distance Telecommunications Policy Rationality on Hold, Pub. Util. Fort., Dec. 22, 1988, at 21-22.

Although the Petitioner may argue that the nascent long-distant competitors installed even minimal facilities, the theory underlying the development of competition in the long-distance market is equally applicable to the instant proceeding. The issue is whether competition will develop if would-be competitors are forced to sink highly expensive redundant networks into the ground before a sufficient customer base has been developed. For the reasons discussed above, total reliance on UNE-loop-based systems is not an economically feasible option. For the purposes of developing local competition, UNE-P, as the Commission has found and as the Supreme Court has upheld, is a sensible and legally sustainable approach. The success of market share building through low-cost entry has been proven in the long-distance market, and the Petitioner here seeks to stifle the consumer benefits similar to those that have accrued in the long-distance market before they can be made available to the local exchange public. Additionally, the provisioning of UNE-P forces carriers toward *cost-based* rates and services, a consumer benefit that cannot be denied. This imperative is enforced by the fact that the Petitioner controls bottleneck facilities whose availability is crucial to competition, and is underscored by the fact that ratepayers paid for the underlying public switched telephone network over time.

**IV. THE COMMISSION SHOULD REJECT VERIZON S ATTEMPT TO REVISE THE MANNER IN WHICH ACCESS CHARGES ARE ASSESSED.**

Verizon urges the Commission to eliminate the current practice in which the UNE-P CLEC collects access charges from the Interexchange Carriers ( IXC ) to originate and terminate long distance traffic on the UNE-P line. Specifically, Verizon asks that the Commission forbear from the current rule that entitles UNE-P carriers to collect per minute

access charges from IXC's. According to Verizon, the CLEC that purchases UNE-P is acting as a marketer of local service while using the incumbent facilities, and it is the incumbent that continues to provide the exchange access services for the call. Verizon also asserts that because exchange access charges were designed as a way to pay for the network infrastructure used in providing local and long distance service, the incumbent should receive the per minute access charges so that the underlying network provider receives the payments that were intended to support the ongoing operation and maintenance of the network.<sup>55</sup> Verizon argues further that its request is otherwise consistent with Section 251(g) of the Act, which expresses Congressional intent that the Act should not disrupt the pre-existing access charge regime under which the local network was built. Yet, the Ratepayer Advocate notes that *ratepayers* paid for the network.

The Commission has already addressed, and settled, the issue of which carrier recoups access charges, and stated that CLEC receipt of the access charges would be consistent with the long term outcome in a competitive market.<sup>56</sup> Further, the loss of access charge revenue was foreseen by the Commission to be offset by interLATA revenues that BOCs would receive under Section 271 dispensation.<sup>57</sup>

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<sup>55</sup>/ *Id.* at 14-15.

<sup>56</sup>/ *First Report and Order*, n.2, *supra*, at para. 717. The Commission noted that short-term detrimental effects might result, but nonetheless held that long-term benefits outweigh short-term discomfort.

<sup>57</sup>/ *First Report and Order* at para. 724.

The New Jersey Ratepayer Advocate submits that the *CALLS Order*<sup>58</sup> adopted by the Commission in May 2000 precludes the relief requested by Verizon. In May 2000, the Commission adopted the *CALLS Order*, which raised the subscriber line charge caps for primary residential and single-line business lines through a series of step increases, while simultaneously eliminating the Primary Interexchange Carrier Charge ( PICC ) for all residential and single-line business lines. In addition, the *CALLS Order* adopted a five-year transitional interstate access and universal reform plan based on a proposal made by the Coalition For Affordable Local and Long Distance which included Bell Atlantic and GTE, predecessor companies of Verizon. The initial part of the plan resulted in an immediate reduction of \$2.1 billion in per-minute switched access charges, which the CALLS IXC members agreed to pass through to their customers and proposed target level for further reductions in per-minute access charges.

As a sponsor of the CALLS proposal, Verizon cannot now seek to alter the access charge regime put in place by the Commission in the *CALLS Order*. The *CALLS Order* intended the payment of per minute access charges to remain in place and not be revised further for the five-year period of the plan. Verizon's petition is asking for a major change in the access charge regime and this directly conflicts with its and the other CALLS members commitment to keep the access charge regime in place for five years. As a result, the New Jersey Ratepayer Advocates submits no changes are permissible at this time. Even if changes could be made, any change in access charges would require that all aspects of the *CALLS Order* be revised, including

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<sup>58/</sup> See Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45, 15 FCC Rcd 12962 (2000) (*CALLS Order*), *aff'd in part, rev'd and remanded in part sub nom. Texas Office of Public Utility Counsel v. FCC*, 265 F.3d 313 (5<sup>th</sup> Cir. 2001).

the increases made to the subscriber line charges. A forbearance petition is not the appropriate mechanism to consider such changes. A Notice of Proposed Rulemaking would be required. Therefore, the New Jersey Ratepayer Advocate requests that the Commission deny Verizon's petition as to any proposed change in access charges.

## **V. CONCLUSION**

WHEREFORE the reasons stated above and herein, the New Jersey Ratepayer Advocate respectfully recommends that the Commission dismiss the Petition for failure to make a *prima facie* case or, in the alternative, to reject the Petition.

Respectfully submitted,

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